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DCI/RM 80-2023
14 November 1980

MEMORANDUM FOR THE RECORD

FROM:

SUBJECT: OSD-OMB Interaction on OSD Deflators

1. As part of OMB's informal comments on the RMS Background Paper on FY82 NFIP inflation it was asserted that,

'Based on results of the Coopers-Lybrand study, the OSD inflation rates appear overstated for the following reasons:

- inflation in the aerospace industry is not as high as originally anticipated,
- labor (the major component to RDT&E rates) appears to be a minor contributor to the price increases in the aerospace industry as compared to material prices,
- long lead times on components, a major contributor to inflation in the aerospace industry, has apparently peaked and started to diminish.'

2. Pursuant to informal contacts with Coopers & Lybrand staff, I met with Dr. Mike Soveriegn, Special Assistant to the ASD Comptroller. Soveriegn expressed concern that OMB cited the Coopers-Lybrand study since they had been given only a cursory reading of the preliminary draft and real distress that they had so grossly misrepresented the study findings. He asserted, to the contrary, that the Coopers-Lybrand study demonstrates that OSD deflators, especially in the outyears, are substantially understated, and that this understatement is across the board and especially acute for aerospace industries.

3. I was allowed to read the Coopers-Lybrand study and confirmed Soveriegn's interpretation. The study focuses exclusively on procurement costs, taking cases ranging from F15 aircraft to harpoon missiles to M-113s. They found that for procurement between FY79-80, inflation was running just under 15 percent as compared with budgetary guidance which allowed for only slightly over 6 percent. (The attached chart provides a series of comparisons including consumer and producers' price indices.)

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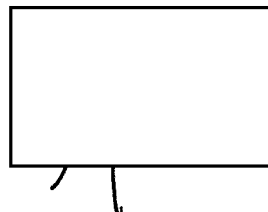
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4. Soveriegn indicated that while OSD and OMB were beginning to see eye-to-eye on each budget year's inflation problem, OMB's insistence on applying unrealistically low outyear inflation rates is having a devastating effect on multiyear DoD procurement and that this was one of the main focuses and findings of the C&L research.

5. Soveriegn expressed interest in the Community Working Group on Inflation and volunteered to make a presentation to the group on the issues of OSD deflators, the Coopers-Lybrand study, and multiyear procurements.

6. Coopers and Lybrand staff members have invited us to their offices to discuss this study for OSD, and I will set this up for next week.

7. All of the above is CONFIDENTIAL.



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Attachment:

Chart: Summary Comparison
Annual Price Increases

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